Opinion **African economy**

African countries should demand loans are made in local currencies

Foreign-denominated debt has a pernicious effect because of rising interest rates

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Nigeria issued $500m-worth of eurobonds in 2011. By 2017, their nominal value had risen to $966m © Bloomberg

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A recent warning by the IMF about rising debt levels in low-income countries has raised questions about the extent to which debt distress is due to lending by China.

The growing debt burden is particularly onerous in Africa. But while China's contribution to that debt is an important issue, it should not be the main focus of policymakers' concern.

There are many reasons to be worried about African debt. It will curtail already depressed growth. It will have a chilling impact on job creation and may lead to a renewed rise in conflict across the continent. It could increase the already substantial migration into Europe and would jeopardise achievement of the UN's sustainable development goals.

These are the probable consequences if a lasting solution to the challenge of balancing growth in Africa with macroeconomic stability is not found. With more than 20 countries on the continent in medium to high levels of debt distress, this is in no one's interest.

Market access is the main driver of recent bulging levels of debt. With African countries needing to accelerate infrastructure development, many sought and obtained access to international capital markets.

Before 2006, only Morocco, Tunisia and South Africa had issued sovereign bonds denominated in foreign currencies. This number grew to 14 by 2017.

In 2018 alone, African countries have sold $18.3bn-worth of euro and dollar-denominated debt. The frequency of bond issuances has also increased. As a result, about 70 per cent of Africa's foreign debt is denominated in dollars or euros. While some analysts link rising debt levels with lending by China, Chinese liabilities in fact accounts for less than 10 per cent of Africa's total external debt.

In an environment of tightening financial conditions, a rising dollar and heightened global protectionism, foreign currency-denominated debt has a pernicious effect on the debt service burden as interest rates rise.

The Ghanaian cedi and the Nigerian naira, for example, have been depreciating against the US dollar since 2008. This means that the current nominal values of the eurobonds issued by both countrieshave increased significantly. In the case of Ghana, the nominal value of its $750m 2007 eurobond was $3.4bn in 2017.

A similar trend is discernible in the case of Nigeria, which issued $500m-worth of eurobonds in 2011. By 2017, their nominal value had risen to $966m.

Is this a poisoned chalice? Is debt denominated in foreign currency a sustainable option for African states?

Many countries are increasingly moving to debt denominated in their local currency, thereby lowering exposure and exchange risks. The decision of India, for example, to borrow mostly in local currency for infrastructure financing through rupee-denominated " masala bonds" is a good example of this strategy.

African countries should — and no doubt will — keep going to the market to finance their growth. However, governments and international financial institutions have a role to play to ensure that this is done in a prudent manner.

Countries should demand that a significant majority of their loans, both market and concessional (that is, loans extended on terms more generous than those offered on the open market), be denominated in local currency.

Second, international financial institutions should come up with ways of hedging their exchange risks as they lend in local currency.

As for African policymakers, a return to prudent macroeconomic management, the development of local capital markets and better regulated financial markets are all ways of ensuring that their countries attract more capital while managing their debt burden.

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